

A cooperative telephone company deriving more than 85 percent of its income from members is exempt under section 501(c)(12) of the Code notwithstanding that nonmembers are charged a higher rate for service than the members.

Advice has been requested whether a cooperative telephone company operated as described below is exempt from Federal income tax under section 501(c)(12) of the Internal Revenue Code of 1954.

The telephone company furnishes services to its members on a cost basis. It also provides services for nonmembers. Charges to nonmembers are substantially higher than charges to members for similar services. More than 85 percent of the company's income is from amounts collected from its members.

Section 501(c)(12) of the Code provides for the exemption from Federal income tax of mutual or cooperative telephone companies, or like organizations, but only if 85 percent or more of the income consists of amounts collected from members for the sole purpose of meeting losses and expenses.

The underlying principle of mutual cooperative operation under section 501(c)(12) of the Code requires that services be provided to members at no more than cost.

Neither section 501(c)(12) of the Code nor any of its predecessors requires a cooperative exempt under section 501(c)(12) to treat both members and nonmembers alike. Furthermore, there is nothing in the legislative history to indicate that such was the intent of Congress. Since the company provides services to its members on a cooperative basis, at no more than cost, and at least 85 percent of its income is received from its members for the sole purpose of meeting losses and expenses, it is held that the company is exempt from Federal income tax under section 501(c)(12) of the Code, notwithstanding that it provides services to nonmembers at prices higher than those charged to members.

Even though an organization considers itself within the scope of this Revenue Ruling, it must file an application on Form 1026, Exemption Application, in order to be recognized by the Service as exempt under section 501(c)(12) of the Code. The application should be filed with the District Director of Internal Revenue for the district in which is located the principal place of business or principal office of the organization. See section 1.501(a)-1 of the Income Tax Regulations.